WILARY WINN LLC

Advice to Strengthen Financial Institutions

Accounting for Credit Union Mergers

Released December 2016 – Version 3

INTRODUCTION

Credit unions historically accounted for mergers under the pooling of interest method. The accounting was relatively straightforward and was accomplished by combining the book values of the two entities. Beginning in 2009, FASB required credit union mergers and acquisitions to be recorded at fair value, making the accounting much more difficult.

Since the new purchase accounting rules became effective, we have worked on over 250 merger and acquisition transactions of all sizes. This white paper is designed to share what we have learned along the way and to address the most common questions we encounter. We hope you find it useful.

We begin with accounting requirements on Day One – the opening journal entry. Next, we discuss the rules for Day Two – the ongoing accounting. Finally, we discuss assessing the goodwill for potential impairment.

KEY TAKEAWAY
We are the number one provider of credit union merger fair value determinations, providing us with deep insight and knowledge of the marketplace. Nationally recognized experts, we combine sophisticated financial expertise with a thorough understanding of the required accounting and have led trainings on the subject for the NCUA. Our white papers have been downloaded thousands of times.

HOW CAN WE HELP YOU?
Founded in 2003, Wilary Winn LLC and its sister company, Wilary Winn Risk Management LLC, provide independent, objective, fee-based advice to nearly 600 financial institutions located across the country.

We provide the following services:

CECL & ALM
Holistic solutions to measure, monitor and mitigate interest rate, liquidity, and credit risk on an integrated basis.

MERGERS & ACQUISITIONS
Independent, fee-based determinations of fair value for mergers and acquisitions.

VALUATION OF LOAN SERVICING
Comprehensive and cost-effective valuations of servicing arising from the sale of residential mortgage, SBA 7(a), auto, home equity and commercial loans.

ADDITIONAL SERVICES
Services to support our CECL, ALM, Fair Value and Loan Servicing product offerings.

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

Accounting for Credit Union Mergers

FAS ASC 805 requires credit unions to use purchase accounting and to record the transaction at fair value. This requires the determination of the fair value of the credit union to be merged in ("acquired credit union") and of all its assets and liabilities. The valuation must also include potential intangible assets such as the core deposit intangible. The fair value estimates must be made in accordance with the requirements of FAS 157 (FAS ASC 820 Fair Value Measurements and Disclosures). Please refer to Appendix A for a comparison of the "old" rules to the "new" rules.

Wilary Winn notes that the purchase accounting rules can apply to a transaction that is not a full merger, including branch acquisitions, purchase and assumption agreements, etc.

Day One Accounting

The acquiring credit union must undertake several steps in order to have the information needed to record the transaction.

It must determine the:

- Overall value of the acquired credit union;
- Fair value of the acquired credit union's financial assets and liabilities;
- Fair value of the acquired credit unions non-financial assets and liabilities; and
- Fair value of any intangible assets – the most common being the core deposit intangible.
- Value of the Tradename
- Amount of Goodwill/Bargain Purchase Gain resulting from the transaction.

OVERALL VALUE OF THE ACQUIRED CREDIT UNION

Valuation experts generally use income-based and market-based approaches to determine fair value. The values derived using the different methods must be reconciled to reach an overall fair value conclusion.

INCOME APPROACH

To determine the fair value of an entity using an income approach, business appraisers generally first estimate the organization's probable future cash flows. They then discount the cash flows back to the valuation date at an appropriate discount rate. However, Wilary Winn believes that the use of future cash flows is not a reliable indicator of value for financial institutions because items like capital expenditures, working capital and debt are not clearly defined. As a result, we base our analysis on future earnings. Wilary Winn uses an approach that is based on a detailed review of the credit union's recent financial performance. We note that the future earnings to be used for this determination are the earnings that the acquired credit union could generate as a standalone entity and should be based on the assumptions used by market participants.

This means that the fair value of the acquired credit union can be different than its value to the acquirer.

For example, for purposes of the valuation, it cannot necessarily be assumed that the acquired credit union costs will go down due to economies of scale, whereas an acquiring credit union could assume this will happen as it builds its internal projections.

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

To determine value under an income approach, we work with our clients to estimate future earnings by developing pro-forma balance sheets and income statements for at least five, and often 10 years, into the future. A key valuation assumption is the rate of future growth. To estimate future growth, Wilary Winn begins with the credit union's historic growth rate and then adjusts it based on any changes in the credit union's field of membership and any significant demographic changes in the area in which the credit union is located. Other key assumptions include:

- Net interest margin – which is dependent on the loan and share mix and future market interest rates
- Non-interest income
- Non-interest expense – the highest cost here is personnel
- Loan loss provision

The key metrics we consider as we develop our pro-formas are:

Capital Adequacy

- Net worth

Profitability

- Return on assets
- Return on equity
- Earning assets to total assets
- Non-interest expense to total assets
- Efficiency ratio
- Assets to employee ratio

Asset Quality

- Non-current loans to total loans
- Loan loss reserve to total loans
- Provision for loan loss to total loans
- Loan loss reserve to non-performing loans
- Net charge-offs to total loans

Liquidity

- Loan to deposit ratio
- Loan to total assets ratio
- Investments to total assets ratio

Wilary Winn notes that a portion of the future earnings are often required to be held in the organization in order for the organization to maintain adequate capital as it grows. This portion would not be available to dividend out, and therefore, we exclude this portion from the present value calculation of future earnings.

Our final steps under the income estimation approach are to discount these earnings back to the valuation date and to estimate the value of the residual. Wilary Winn uses a Capital Asset Pricing Model ("CAPM") approach in order to determine the discount rate to use in our income approaches. We generally rely on the Duff & Phelps Valuation Handbook Industry Cost of Capital. We note that the Duff & Phelps cost of capital is based on after-tax cash flows. Wilary Winn uses the after-tax cash flow discount rate because credit unions do not pay income taxes and have, as an industry, passed this benefit on to their members by offering lower rates on loans and higher rates on deposits than their commercial banking competitors. Thus, we believe the earnings themselves reflect the tax effect and that the use of an after-tax discount rate is appropriate.

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

MARKET APPROACHES

In addition to the Income Approach, we utilize two market approaches – Guideline Transaction and Market Value. Under the Guideline Transaction approach, we obtain deal results and financial information for recent bank acquisitions of similar size and in similar geographic areas to credit unions we are valuing. To obtain our estimate of value, we use the median price to tangible book value from our pool of deal results and adjust for differences in profitability.

Wilary Winn bases the market approach on market values of publicly traded community banks. To estimate the equity value of the credit union, we identify the price to earnings and price to book ratios for banks with similar asset size in the same geographic area. We then adjust for differences in return, growth, and a market control premium.

Finally, we reconcile the valuation estimates derived under the three methods and determine the overall fair value of the acquired credit union. We note that we weight the income approach the highest, as we believe this method is most representative of the entity value. The capital in excess of the 7% required by the NCUA to be "well capitalized" of $8,223,000 is removed from the projections, as we do not believe a market participant would pay a premium for this excess capital. The excess capital is added back dollar-for-dollar to the value derived from the three approaches, as shown in Appendix B.

The overall fair value estimate is the amount of equity that can be recorded on Day One. See the $29,198,000 in the example valuation summary attached as Appendix B.

FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

The financial assets and liabilities consist primarily of loans, investments and shares. Accrued interest receivable, accounts receivable, accrued interest payable and accounts payable are also considered to be financial assets or liabilities.

INVESTMENTS

Investments generally consist of certificates of deposits and "vanilla" bonds. To determine the value of a CD, Wilary Winn discounts the expected cash flows using an estimated market interest rate over its expected remaining life. We can generally identify a price for the bonds using Bloomberg or another pricing service. We occasionally encounter illiquid securities, which we value using discounted cash flows.

ACCOUNTS RECEIVABLE AND PAYABLE

Wilary Winn generally values the short-term accruals, accounts receivable and accounts payable at book value, because we believe the present value effect is immaterial.

SHARES

The fair value of the share accounts is dependent on whether they are time or non-time deposits. The non-time share deposits are recorded at book value. The value of the non-time deposits is reflected in the "core deposit intangible". The valuation of intangible assets is discussed beginning on page 6.

Wilary Winn estimates the value of time deposits in a manner similar to the one we use for certificate of deposit investments.

LOANS

Wilary Winn believes determining the fair value of the loans is one of the most complex undertakings under the purchase accounting rules. The marketplace for seasoned loans is not active. As a result, valuation experts generally value the loans using a discounted cash flow analysis. Two approaches are permissible

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

under GAAP[1]. One approach is to discount the contractual cash flows at an "all in" estimated market discount rate, which by its nature includes a credit spread. The other approach is to develop a "best estimate of expected cash flows" and discount the amounts back to the valuation date at an appropriate discount rate. We estimate the value of the loans based on their contractual interest rate and their probable lifetime credit losses, by performing a discounted cash flow analysis using a proprietary valuation model. The valuation is performed at the loan level for all loans secured by real estate and at the cohort level for all other loans and is based on the objective attributes of the loans in the portfolio (i.e., the rate of interest on the loan, the original term of the loan, the current term of the loan, etc.) and current statistical performance variables used in the marketplace. Our analysis is based on the contractually specified amounts of principal and interest to be received, ***modified by our estimates*** of prepayment, default and loss severity to be experienced prospectively. Our prepayment, default and loss severity assumptions are applied at the loan or cohort level based on the characteristics of the loan (type of loan – new car, FICO – prime, non-prime, sub-prime, etc.).

We generally use the "all in" market interest rates to discount the expected cash flows for loans with FICO scores above 720, as our estimated credit loss estimates for these loans are generally quite modest. In other words, our best estimate cash flows are very similar to the contractual cash flows, implying that the amount of credit spread included in the discount rate is also quite modest. On the other hand, for loans with scores below 720, we use the buildup method to develop our discount rate. We begin with an appropriate risk-free rate based on the term of the loan (adjusted for amortization, voluntary, and involuntary prepayments), and add a spread for uncertainty and liquidity. Because we are using expected cash flows net of credit losses, our discount rates for loans with FICOs under 720 do not include a credit spread. Wilary Winn believes including the credit spread in the discount rate for these loans with lower credit quality would be "double counting".

The book value of the loans is thus adjusted for an interest rate differential (discount rate valuation allowance) and the present value of expected credit losses (credit valuation allowance).

Due to the estimated fair value of the loans including the estimated credit losses, the allowance for loan losses is recorded at zero on day one.

See the adjustments to loans in the example loan summary attached as Appendix C – the interest rate premium – $102,380 in total and the credit loss discounts – $1,188,864 in total. See the Day Two accounting section of this white paper for more details.

PREPAID EXPENSES

The treatment of prepaid expenses is another item that is less straightforward than one would imagine. One has to consider whether the prepaid item would have benefit to market participants. For example, a multi-year prepaid contract that cannot be used after the merger would have no "fair value" and would be recorded at zero in the Day One journal entry.

ACCRUED LIABILITIES

Wilary Winn recognizes that prior to the change in the accounting rules, many acquiring organizations had the acquired credit union accrue the costs of the merger on its book prior to the merger so the expenses would not flow through the income statement of the combined entity. This is another significant change under the new rules.

---

[1] FAS ASC 820-10-55-4

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

In general, the costs of the merger and any restructuring costs should flow through the income statement of the acquiring credit union[2].

The theory is that if the party that receives the primary benefit is the buyer or the combined entity, the cost should run through its income statement. In our experience, the types of costs that can be accrued as part of the merger are quite limited. An example would be a compensation arrangement that was in place before the merger was contemplated, and that just happens to be triggered as a result of the merger. The required payout can be accrued on the acquired credit union's books as of the merger date. By way of contrast, a payout negotiated as part of the merger should run through the income statement of the acquiring credit union.

The acquiring credit union should also ensure that the acquired credit union has properly accrued its expenses. In other words, the organization should ensure that the acquired credit union does not have any unrecorded liabilities.

FAIR VALUE OF NON-FINANCIAL ASSETS AND LIABILITIES

The most significant non-financial assets are generally land and buildings. We generally require our clients to obtain commercial real estate appraisals if these assets are material.

Real estate leases are another item that must be evaluated in a merger. If the lease price is less than the market rate, then an asset should be recorded. On the other hand, if the lease price is over the market rate, a liability should be recorded. We calculate these items by discounting the difference in cash flows back over the remainder of the lease term to the valuation date at the acquired credit union's estimated cost of capital.

INTANGIBLE ASSETS

The value of intangible assets should be recorded as well in the Day One journal entry.

Recognition of an intangible asset requires that the asset be separable or have a contractual or legal benefit.

The most common intangible assets in a credit union merger are:

- Mortgage servicing rights
- Core deposit intangible
- Member relationships
- Value of the acquired credit union's trade name

MORTGAGE SERVICING RIGHTS

Mortgage servicing rights are the rights to service a loan that has been sold into the secondary market in exchange for a fee. The market for bulk sales of mortgage servicing rights is quite limited. As a result, the value of mortgage servicing rights is generally determined via a discounted cash flow analysis. The most sensitive input in the valuation is the assumption regarding the rate at which the loans will prepay.

---

[2] FAS ASC 805-10-25-23

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

CORE DEPOSIT INTANGIBLE

The premise underlying the core deposit intangible asset is that a rational buyer would be willing to pay a premium to obtain a group of core deposit accounts that are less expensive than the buyer's marginal cost of funds. Wilary Winn believes the core deposit intangible benefit depends on the type of account. For example, share drafts accounts have very different economics and behavior than high-rate money market shares. To calculate the estimated fair value of the core deposit intangible, we first segment the accounts by type. Next, we estimate the likely decay, average life, and terminal economic life. The rate paid on the deposit, the non- interest income generated, and the non-interest expense incurred also affect the value of the core deposit intangible. Wilary Winn estimates the value of the core deposit intangible through a discounted cash flow analysis.

MEMBER RELATIONSHIPS

Wilary Winn believes that the value of the member relationships is imbedded in the overall value of the entity and the core deposit intangible. We believe it would be quite difficult to separately determine the value of member relationships in terms of the ability to cross sell loans or shares at lower cost, or higher rates of penetration, and therefore, have generally not seen such items recorded.

ACQUIRED CREDIT UNION'S TRADE NAME

A trade name can have value based on how widely it is recognized. If the brand is well known and the acquiring credit union intends to continue to utilize it, the trade name has value. Trade names can also have a defensive value. That is, it can have value even though the acquiring credit union plans to retire the name. For example, imagine the value to Pepsi of having the rights to the Coca-Cola brand name.

GOODWILL OR BARGAIN PURCHASE

On Day One, the acquiring credit union records the overall fair value of the acquired credit union, the fair value of the assets acquired and liabilities assumed, and the fair value of any intangible assets.

The amount required to balance the Day One journal entry is Goodwill or a Bargain Purchase. Wilary Winn believes a merger transaction will generally result in goodwill, as opposed to a bargain purchase gain.

In fact, GAAP requires the acquiring credit union to "double check" its work before recording a bargain purchase[3].

The resulting goodwill can be amortized as it was under the old rules. Alternatively, it can remain on the balance at recorded value subject to annual impairment testing, the details of which are contained later in this white paper.

See Appendix B for an example comparing the fair value of the balance sheet to the book value at the merger date. Appendix D shows how to record the acquisition on Day One, including the accounts used to adjust book value to fair value.

See Appendix D for an example of the Day One journal entry to record the merger.

---

[3] 3 FAS ASC 805-30-25-4

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

Wilary Winn further notes that GAAP allows the acquiring credit union to true up the Day One journal entry for up to 12 months after the merger date to reflect new information that would have affected the valuation amounts had they been known[4].

We note that the "new" information is relative to the acquisition date only. The adjustment is designed to reflect information that existed as of the valuation date that was not known at the time. It is not intended to reflect changes in facts and circumstances as of the valuation date. Instead, it is designed to reflect a clarification of facts that existed as of the valuation date. For example, if a loan at the valuation date was a modified loan and was not disclosed as such, an adjustment would be appropriate. On the other hand, if the acquired credit union obtained an appraisal for a branch location at the acquisition and due to changes in market conditions, the value of the branch was less 11 months later, an adjustment would not be appropriate.

Regulatory Reporting – 5300 Call Report

For regulatory reporting purposes, the acquiring credit union does not include the equity acquired in the merger (the overall fair value of the acquired credit union – the $29,198,000 in our example included as Appendix B). Instead, it reports the acquired credit union's retained earnings as of the valuation date – the $24,799,000 in our example attached as Appendix B.

Thus, for regulatory capital purposes, the acquiring credit union is able to count the acquired credit union's book equity.

For GAAP purposes, the equity acquired in the merger is reported in the Equity Section on line 33. The amount on line 33 is not carried over to the PCA Net Worth Calculation Worksheet. Instead, the acquired credit union's retained earnings are reported on line 7b of the Worksheet[5]. See Appendix D for more details.

We further note that in the case of involuntary, regulatory-assisted mutual to mutual credit union combinations, the amount of regulatory capital flowing to the acquiring credit union is zero. In other words, the acquired credit union's retained earnings as of the valuation date do not count toward regulatory capital.

Finally, in our experience, the external auditors will specifically perform a review as of the acquisition date to ensure that the amount of regulatory capital reported is in accordance with GAAP. For example, they will ensure that all liabilities that should have been recorded have been recorded and the allowance for loan losses has been calculated properly in accordance with GAAP.

GOODWILL AND BARGAIN PURCHASE GAINS

Any goodwill recognized in a business combination is recorded on line 31.b of the Statement of Financial Condition. Any gain recognized from a bargain purchase should be reported on line 16 of the Statement of Income/Expense.

Wilary Winn notes that any assistance provided by the NCUA is recorded as a reduction of goodwill. Assistance would result in a bargain purchase only if the amount of the assistance exceeded the goodwill and the gain would be only the excess amount. We further note that the amount of bargain purchase gain

---

[4] FAS ASC 805-10-25-13
[5] 12 CFR Part 702.2 (f) (3)

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

must be deducted from the combined entity's retained earnings when calculating regulatory capital. We note that this reduction is subject to a floor of zero. In other words, if the bargain purchase is greater than acquired credit union's net worth, the acquiring credit union would reduce regulatory capital by the amount of acquired credit union's retained earnings only[6].

We further note that the amount of goodwill, subject to certain phase-in provisions, will not count toward risk-based regulatory net worth when the rule becomes effective on January 1, 2019.

DELINQUENCY STATUS OF PURCHASED LOANS AND OTHER FINANCIAL ASSETS

The delinquency status of purchased loans and other purchased financial assets must be determined in accordance with the contractual repayment terms for the purposes of reporting on delinquency schedule of the 5300. The delinquent loan should be reported at its recorded amount and not at its contractual balance due[7].

NONACCRUAL STATUS OF PURCHASED IMPAIRED LOANS

Normal nonaccrual parameters apply to purchased impaired loans.

Day Two Accounting

Many find the Day One Accounting to be relatively complex. The ongoing accounting for the recorded premiums and discounts is also quite complex. The following is a quick summary for the items other than loans, followed by a detailed description of the required ongoing accounting for the acquired loans.

The premiums or discounts for the investments acquired are amortized or accreted into income over the estimated life of the investment as an adjustment to interest income. Premiums reduce interest income, whereas discounts have the opposite effect.

The premiums or discounts on the acquired time deposits are amortized or accreted into expense over the estimated life of the liability as an adjustment to interest expense. Premiums reduce interest expense, whereas discounts increase interest expense.

Mortgage servicing rights acquired in the merger are generally amortized on a level-yield basis over the estimated life of the loans. The amortization is recorded as a reduction to servicing income. We note that mortgage servicing rights can also be measured and reported on an ongoing basis at fair value, with the change in fair value running through the income statement. This fair value accounting is generally used by large institutions, which have generally hedged the portfolio against interest rate risk.

The core deposit intangible is amortized on a level-yield over the estimated lives of the non-time deposits. The expense should be recorded as a reduction to non-interest income.

---

[6] 12 CFR Part 702.2 (f) (3)

[7] Interagency Supervisory Guidance on Bargain Purchases and FDIC- and NCUA-Assisted Transactions – June 7, 2010

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

The fair value of the fixed assets acquired becomes the basis for depreciation. The fixed assets should be depreciated over their estimated remaining lives, which can be longer or shorter than the term used to calculate depreciation before the acquisition.

The most complex ongoing accounting relates to the acquired loans. The required accounting centers on two questions.

1. Do I account for the loans at based on their *contractual* cash flows, or
2. Do I account for loans based on their *expected* cash flows

CONTRACTUAL CASH FLOWS

If the acquiring credit union expects to receive all the contractually specified principal and interest payments from an acquired loan, then the loan should be accounted for in accordance with ASC 310-20. That is, the interest rate discount or premium (interest rate valuation allowance) should be amortized or accreted into income on a level-yield over the expected life of the loan. Under this method, the acquiring credit union establishes a *post-acquisition* allowance for loan losses to record credit losses on acquired loans.

Wilary Winn believes that the acquiring credit union can account for the acquired loans with the highest credit quality (FICOs over 720, reasonable LTVs) using this methodology. We note that our estimated credit losses for these types of loans are generally quite nominal and that we use an adjusted market discount rate to estimate fair value. Thus, the valuation approach and the accounting are consistent. The acquiring credit union amortizes the interest rate valuation allowance and the relatively modest credit valuation allowance into income over the expected life of the loan.

EXPECTED CASH FLOWS

On the other hand, loans acquired with "deteriorated credit quality" must be accounted for under ASC 310-30 (pre-codified Statement of Position 03-3 *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*).

WHICH LOANS FALL WITHIN THE SCOPE OF ASC 310-30?

Acquired loans that meet the following two criteria must be accounted for pursuant to ASC 310- 30:

1. There must be evidence of deterioration in credit quality ***subsequent to origination***.
2. It must be probable that the acquirer will be unable to collect all contractually required payments from the borrower.

The determination of whether acquired loans are to be accounted for under ASC 310-30 must be made at the acquisition date on a loan-by-loan basis, and loans cannot transition between ASC 310-30 and ASC 310-20 subsequent to the acquisition date.

REQUIREMENT 1 – DID THE DETERIORATION IN CREDIT QUALITY OCCUR SUBSEQUENT TO ORIGINATION?

At first glance, this determination may appear simple. One can review the loan's performance and underlying attributes to determine whether credit concerns exist. Factors to consider are the borrower's credit score, sources and uses of cash, payment history, and debt-to-income levels. However, to qualify for accounting under ASC 310-30, this deterioration in credit quality must have occurred subsequent to origination. Accordingly, a loan that was of lower credit quality from the time of its origination may or may not fall into the ASC 310-30 bucket. If the loan has continued to perform based on its contractual terms, then chances are good that deterioration in credit quality did not occur subsequent to acquisition.

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

To be eligible for ASC 310-30, the credit conditions would have had to have worsened – the credit score fell, the loan to value ratio increased, etc.

REQUIREMENT 2 – IS IT PROBABLE THAT THE ACQUIRER WILL BE UNABLE TO COLLECT ALL CONTRACTUALLY REQUIRED PAYMENTS FROM THE BORROWER?

Wilary Winn believes that if the fair value of the loan includes a credit valuation allowance, it is clear that the acquirer will not receive the contractually required payments from the borrower. We further believe that high FICO, low loan to value loans will generally not have a significant credit valuation allowance and would thus fail this requirement, whereas the remainder of the portfolio would likely meet this requirement.

Thus, loans with credit valuation allowances clearly meet Requirement 2, but may not meet Requirement 1. Fortunately, GAAP permits the acquiring credit union to elect to account for the loans at the group level, thus avoiding the tedious scope determination required under Requirement 1[8].

Wilary Winn thus recommends that the acquiring credit union make two accounting elections for loans that have credit valuation allowances which are material.

1. Account for the acquired loans at the group level.
2. Elect to treat the group level asset in accordance with ASC 310-30.

We believe this dramatically simplifies the ongoing accounting, ***provided that you can differentiate between the fair value adjustments for the interest rate differential and the expected credit losses.***

Wilary Winn believes that the acquiring credit union could also elect to include loans with the highest credit quality as it forms the loan groups. For example, an acquiring credit union could elect to account for all the first lien residential mortgage loans acquired as a group based on expected cash flows versus accounting for the loans with the highest credit quality using contractual cash flows. We note that the loans should be grouped based on similar characteristics - residential first lien, residential second lien, new direct auto, used indirect auto, etc.

Wilary Winn further notes that it is “worth the effort” to determine whether to account for relatively large member business loans at the loan level and go through the process of determining whether the particular loan should be accounted for under ASC 310-20 or ASC 310- 30.

We note that GAAP does not allow loans with revolving terms to be accounted for under ASC 310-30 because of the uncertainty of future advances and repayments[9]. In our experience, the acquiring credit union amortizes the discount rate valuation allowance and the credit valuation allowance straight-line over the remaining term of the loan as of the acquisition date of the loan. If it becomes apparent over time that the present value of the cash flows is less than the book value of the loan, then the acquiring credit union should increase its allowance for loan losses by the amount of the shortfall.

RECOGNIZING INCOME UNDER ASC 310-30

Under ASC 310-30, the expected cash flows that exceed the initial investment in the loan (its fair value on Day One) represent the “accretable yield,” which is recognized as interest income on a level-yield basis over

---

[8] AICPA Depository Institutions Expert Panel Letter to SEC December 18, 2009
[9] ASC 310-30-15-2 (f)

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

the life of the loan. Appendix C compares the book values to the fair values by loan group and details the interest rate and credit reductions. Using the Used Vehicle – Direct loans as an example, the interest rate difference is $65,348 and the credit only difference is $127,337. The book value is $12,500,000, and based on the interest rate and credit reductions, the fair value is $12,307,315. Under ASC 310-30, the acquiring credit union would accrete the $12,307,315 fair value at a rate of 3.8%. Actual interest and principal received would be accounted for as a reduction of the fair value carrying amount of the loan.

In our experience, our client's core accounting systems cannot accommodate the precise accounting required under ASC 310-30. In response, we separately identify the present value of the difference between the expected cash flows at the coupon rate and the expected cash flows at the market rate of interest. This is the interest rate premium (discount rate valuation allowance) or the $65,348 in our used direct vehicle loan example. We advise our clients to amortize the discount rate valuation allowance into income using the sum-of-the-years' digits amortization (which closely resembles level-yield amortization). Since the discount rate valuation allowance is based on the *difference* between the rate on the portfolio and the overall market interest rate, our clients can continue to record the contractual interest income as received and continue to rely on their core system to provide the loan-by-loan accounting. The result very closely approximates the precise accounting required under ASC 310-30. Appendix E compares accreting the discount rate valuation allowance using the sum-of-the years' digits method and recording the contractual cash flows as received to the required accretion required ASC 310-30 for the used direct vehicle loans in our example. The schedule shows that the interest income recorded would be slightly higher than the interest income recorded under the exact ASC 310-30 accounting for the first 36 months and then is slightly less for the next 10 months. Our clients have found in practice that the simplicity of this amortization method outweighs the modest differences produced, as compared to the cumbersome reporting required using a precise implementation of the standards.

Wilary Winn strongly recommends that this simplified approach not be used to account for large member business loans with significant credit valuation allowances. We recommend that such loans be accounted for at the loan level in accordance with the precise tenets of FAS ASC 310-30. For more information, please see our white paper *FAS ASC 310-30 Loan Accounting*.

Wilary Winn further notes that the difference between the cash flows expected at acquisition and the total contractual cash flows is the nonaccretable difference. The nonaccretable difference is the undiscounted principal and interest that will not be received due to prepayment and default assumptions. In our used direct loan example, the amount is $442,016. We note that the total contractual cash flows must be disclosed only once and need not be tracked going forward.

Finally, we note that examples of templates used to amortize/accrete the fair value adjustments for all the accounts, including the loan adjustments, are attached as Appendix F.

CHANGES IN ESTIMATES OF CASH FLOWS UNDER ASC 310-30

The acquiring credit union must periodically compare the actual cash flows received to the expected cash flows on Day One and reassess the remaining cash flows expected to be collected. If the new total expected cash flows exceed the initial estimate, then the acquiring credit union should increase the rate of accretion. In essence, the fair value of the loan has increased, but the increase can only be recognized prospectively through an increased yield. If the expected cash flows have decreased, then the acquiring credit union should record an allowance for loan losses.

Because the allowance for loan losses is initially recorded at zero with expected credit losses reflected in the credit loss valuation allowance, the tracking and reporting of credit losses is more complex under the new rules. Some organizations have charged foreclosure losses directly against the credit loss valuation allowance. In our experience, the NCUA prefers to see losses run through the allowance for loan losses and

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

related provision accounts. In this case, Wilary Winn recommends that foreclosure losses be recorded through the three following journal entries. In our example, we assume a foreclosure loss of $100.

Allowance for loan losses	100	
Loan receivable		100

Provision for loan losses	100	
Allowance for loan losses		100

Credit reserve valuation allowance	100	
Other non-interest income		100

The net effect of these entries with regard to profit and loss is zero. However, the actual foreclosure losses incurred are easier to track because they run through the standard accounts. We note that the final credit should run through other non-interest income, not interest income, because the entry is designed to offset the provision expense and is not meant to reflect an adjustment to the prospective yield.

We further recommend that the acquiring credit union allocate the carrying amount of the foreclosed loan based on the individual loan's relative initial fair value. This method mirrors traditional loan accounting and is consistent with the requirements of ASC 310-30. Under this method, a gain or loss would be recognized for the difference between the allocated carrying amount of the loan and the fair value of the collateral obtained in foreclosure. When allocating costs while removing loans from the pool, the accounting principle that should be adhered to is that the yield on the remaining pool should not be disturbed by the removal. That is, the yield on the remaining pool of loans should neither increase nor decrease as a direct result of removing a loan from the pool.

Finally, if the actual cash flows for the loan group differ significantly from the cash flows expected at inception, Wilary Winn recommends that the steps in the Day One valuation be repeated at the new assessment date and that new rates of accretion be calculated or that the allowance for loan losses be increased or decreased depending on whether the new cash flows have increased or decreased.

OTHER RULES RELATED TO THE GROUPED LOANS

Wilary Winn notes that the integrity of the pool should be maintained throughout its life. Thus, loans should not be added to the pool, nor should loans be removed absent events such as foreclosures, write-offs, or sales of the loan[10].

We also believe that the acquiring credit union should not apply troubled debt restructuring accounting and disclosure guidance to loans included in a pooled asset under ASC 310-30[11].

---

[10] FAS ASC 310-30-40-1
[11] FAS ASC 310-40-15-11

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

Accounting For Goodwill

As we indicated earlier, the goodwill recorded in a merger transaction can be amortized or the carrying amount can remain on the balance sheet subject to annual impairment testing.

If a credit union elects to amortize the goodwill, the amount can be amortized over a period not to exceed 10 years.

Wilary Winn cautions that in order to use this method, the credit union must make an irrevocable accounting election. The election affects the existing goodwill, as well as any additional goodwill acquired in the future[12].

If the credit union does not make the election to amortize the goodwill, it is subject to annual impairment testing. The process begins by determining the entity to be assessed. Perhaps counter-intuitively, the goodwill test is nearly always performed at the combined entity level instead of at the level of the acquired credit union. The test would be performed at the acquired credit union level only if it were deemed to be a separate operating segment or a component of a separate operating segment. An entity must have all the following characteristics to be deemed a separate operating segment[13]:

- It engages in business activities from which it may earn revenue and incur expenses;
- Its *discrete financial information is available*; and
- Its operating results are *regularly reviewed* by the chief operating decision maker ("CODM") to make decisions about *resources to be allocated* to the segment and assess its performance.

Wilary Winn believes it would be rare for an acquired credit union to be considered a separate operating segment. This implies that the branches of the acquired credit union would have separate pricing, separate asset liability management, etc. We further believe that over time members will migrate from the acquired credit union's branches to the acquiring credit union's branches and vice versa, further clouding the distinction.

The assessment for goodwill impairment can be qualitative or quantitative.

QUALITATIVE TESTING

A credit union may assess qualitative factors to determine whether it is more likely than not (that is, a likelihood of more than 50 percent) that the fair value of the reporting unit is less than its carrying amount, including goodwill. In evaluating performing, the qualitative test the guidance requires an entity to assess relevant events and circumstances. Examples of such events and circumstances include the following[14]:

- *Macroeconomic conditions*, such as deterioration in general economic conditions, limitations on accessing capital, fluctuations in foreign exchange rates, or other developments in equity and credit markets.

- *Industry and market considerations*, such as a deterioration in the environment in which an entity operates, an increased competitive environment, a decline (both absolute and relative to its peers) in

[12] FAS ASC 350-20-35-62
[13] FAS ASC 280-10-50-1
[14] ASC 350-20-35-3C

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

market-dependent multiples or metrics, a change in the market for an entity's products or services, or a regulatory or political development.

- *Cost factors*, such as increases in raw materials, labor, or other costs, that have a negative effect on earnings.

- *Overall financial performance*, such as negative or declining cash flows or a decline in actual or planned revenue or earnings.

- *Other relevant entity-specific events*, such as changes in management, key personnel, strategy, or customers; contemplation of bankruptcy; or litigation.

- *Events affecting a reporting unit*, such as a change in the carrying amount of its net assets, a more-likely-than-not expectation of selling or disposing all, or a portion of, a reporting unit, the testing for recoverability of a significant asset group within a reporting unit, or recognition of a goodwill impairment loss in the financial statements of a subsidiary that is a component of a reporting unit.

QUANTITATIVE TESTING

If after assessing the totality of events or circumstances described in the paragraphs above, a credit union determines that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, then the credit union must perform the first step of the two-step goodwill impairment test.

Step One is to determine whether the fair value of the combined entity exceeds its book value using the income and market approaches described at the beginning of this white paper. If the fair value of the combined entity exceeds the book value, the goodwill is not impaired[15]. If the combined entity fails Step One, it means the credit union must measure the impairment loss in accordance with Step Two.

In Step Two, the credit union compares the carrying amount of the reporting unit goodwill to the implied fair value of that goodwill and recognizes an impairment loss equal to that excess. The loss recognized cannot exceed the carrying amount of goodwill[16].

Conclusion

While the initial and ongoing required accounting can be complex, Wilary Winn does not believe the rules should deter transactions that otherwise make sense. We have worked with our clients, their external auditors, and the regulators to ensure our clients have the information and knowledge they need to successfully undertake these transactions. We hope you have found this white paper to be informative and useful.

---

[15] FAS ASC 350-20-35-4
[16] FAS ASC 350-20-35-11

Prepared by Wilary Winn LLC - All Rights Reserved - Contact us at info@wilwinn.com - www.wilwinn.com

Appendix A

Issue	Previous Requirement	New Requirement
Definition of a business	Business had to have inputs, processes and outputs	Business does not have to outputs thus expanded scope
Combination of mutual entities including credit unions	Pooling of Interests	Purchase accounting
Allowance for loan and lease losses	Recorded at appropriate amount – book value if correct	Recorded at zero – fair value includes reduction related to credit losses
Assets acquired and liabilities assumed	Record at book value	Record at estimated fair value
Restructuring Costs – involuntary severance, contract termination, etc.	Generally recognized as a liability in connection with the merger	Generally an expense to the combined entity
Adjustments to fair value estimates within one year measurement period	Recognize prospectively	Make changes retroactive to the acquisition
Non-contractual asset or liability contingencies	Account for under FAS 5 – probable and measurable	Record if "more likely than not"
Assets that acquirer does not intend to use	Generally assigned limited or no value	Record at fair value – highest and best use
Bargain Purchase	Extraordinary when fair value of assets (after reduction of certain long term assets to zero) exceeded consideration given	Bargain purchase if fair assets assumed exceeds fair value of liabilities assumed and consideration given
Goodwill	Amortized	Subject to annual impairment testing

XYZ Credit Union
Assets & Liabilities as of *date*

	Balance	Coupon	Market Price	Remaining Term in Months	Estimated Fair Value %	Estimated Fair Value $	Difference
ASSETS							
Cash	24,000,000				100.0%	24,000,000	-
Available for Sale Securities	11,000,000				98.0%	10,780,000	(220,000)
Deposits in Commercial Banks, S&Ls, Savings Banks	3,000,000	1.2%	0.9%	12.9	100.2%	3,006,000	6,000
Total Membership and Paid In Capital	1,000,000				100.0%	1,000,000	-
All Other Investments	400,000				126.0%	504,000	104,000
Total Loans and Leases	181,075,000				99.4%	179,988,516	(1,086,484)
Total Loans and Leases - Loss Allowance	(1,000,000)				0.0%	-	1,000,000
Land and Building	7,500,000				109.0%	8,175,000	675,000
Other Fixed Assets	500,000				100.0%	500,000	-
NCUA Share Insurance Capitalization Deposit	2,000,000				100.0%	2,000,000	-
Accrued Interest on Loans	300,000				100.0%	300,000	-
Accrued Interest on Investments	25,000				100.0%	25,000	-
All Other Assets	7,000,000				100.0%	7,000,000	-
Total Assets	236,800,000				100.2%	237,278,516	478,516
LIABILITIES							
Accrued Dividends & Interest Payable on Shares & Deposit	1,000				100.0%	1,000	-
Accounts Payable and Other Liabilities	3,000,000				100.0%	3,000,000	-
Share Drafts	38,000,000				100.0%	38,000,000	-
Regular Shares	60,000,000				100.0%	60,000,000	-
Money Market Shares	63,000,000				100.0%	63,000,000	-
IRA/KEOGH Accounts without Defined Maturities	5,000,000				100.0%	5,000,000	-
All Other Shares	6,000,000				100.0%	6,000,000	-
Share Certificates	25,000,000	1.1%	0.7%	12.9	100.5%	25,125,000	125,000
IRA/KEOGH Certificates	12,000,000	1.2%	0.8%	16.9	100.5%	12,060,000	60,000
Total Liabilities	212,001,000				100.1%	212,186,000	185,000
EQUITY	24,799,000					25,092,516	293,516

	Base Value	Weighting	Weighted Value
Overall Value of XYZ Credit Union - Income Projected	21,500,000	75%	16,125,000
Overall Value of XYZ Credit Union - Guideline Transaction	19,000,000	15%	2,850,000
Overall Value of XYZ Credit Union - Market Valuation	20,000,000	10%	2,000,000
Overall Value of XYZ Credit Union - Total Wtd Avg		100%	20,975,000
Excess Capital Value Dollar-for-Dollar			8,223,000
Estimated Value of the Franchise			29,198,000
Value of Assets and Liabilities			25,092,516
Value of Core Deposits			2,500,000
Total Liquidation Value of the Entity			27,592,516
Total Estimated Value of the Entity (Max of Income and Market Valuations or Liquidation Value)			29,198,000
Value of Financial Assets and Liabilities			16,417,516
Value of Non-Financial Assets and Liabilities			8,675,000
Value of Core Deposits			2,500,000
Goodwill (Bargain Purchase)			1,605,484

XYZ Credit Union
Loan Valuation as of *date*

	Principal Balance	# of Loans	Avg FICO	Avg LTV*	60+ DQ%	Current WAC	Lifetime WAC	Age	WAM	Avg Life	CPR %	CRR %	CDR %	Severity%	Future Loss %	Risk-Free Discount Rate	Discount Spread	Total Discount Rate	Fair Value %	Fair Value $	Difference	Credit Only Difference[1]	Discount Rate Difference[2]	Contractual Cash Flows	Non-Accretable Credit Losses	Non-Accretable Lost Interest	Total Non-Accretable Cash Flows
Fixed Rate Mortgage	36,000,000	326	738	50%	0.0%	4.0%	4.0%	36	163	4.0	13.6%	12.8%	0.8%	10.6%	0.4%	3.2%	0.1%	3.3%	101.6%	36,586,955	586,955	(135,755)	722,710	47,587,079	135,755	5,668,727	5,804,481
Home Equity 2nd	10,000,000	322	740	60%	0.0%	5.4%	5.4%	29	88	1.9	28.3%	27.8%	0.5%	22.6%	0.3%	5.5%	0.4%	5.9%	99.1%	9,912,094	(87,906)	(25,689)	(62,218)	11,929,719	25,689	1,188,641	1,214,330
HELOC 1st	200,000	1	791	100%	0.0%	4.5%	4.5%	2	11	0.9	20.9%	20.8%	0.1%	15.3%	0.0%	3.6%	0.8%	4.4%	100.1%	200,246	246	(31)	277	229,114	31	146	177
HELOC 2nd	11,000,000	427	750	54%	0.6%	4.5%	4.6%	54	200	2.6	20.1%	19.5%	0.5%	47.8%	0.6%	3.9%	0.8%	4.7%	99.4%	10,932,946	(67,054)	(61,908)	(5,146)	13,222,644	61,908	812,268	874,176
MBL - RE Secured - Fixed	15,000,000	93	759	n/a	0.0%	4.8%	4.8%	29	83	3.5	16.7%	11.8%	4.8%	11.2%	1.3%	4.5%	0.0%	4.5%	98.8%	14,820,330	(179,670)	(197,768)	18,098	22,339,442	197,768	4,621,938	4,819,707
MBL - RE Secured - Adjust.	6,000,000	34	728	n/a	0.0%	4.8%	4.1%	32	106	4.0	14.9%	11.8%	3.0%	10.0%	0.9%	1.4%	2.4%	3.8%	99.4%	5,964,933	(35,067)	(56,961)	21,894	9,283,668	56,961	2,108,161	2,165,122
New Vehicle - Direct	1,500,000	69	737	n/a	0.0%	3.1%	3.1%	19	49	1.5	24.1%	23.6%	0.5%	39.0%	0.3%	3.1%	0.3%	3.4%	99.3%	1,489,380	(10,620)	(4,452)	(6,168)	1,599,856	4,452	28,477	32,929
Used Vehicle - Direct	12,500,000	1,091	707	n/a	0.1%	3.5%	3.5%	14	53	1.6	25.0%	23.4%	1.6%	39.8%	1.0%	3.0%	0.8%	3.8%	98.5%	12,307,315	(192,685)	(127,337)	(65,348)	13,509,212	127,337	314,679	442,016
New Vehicle - Indirect	4,000,000	264	691	n/a	1.4%	4.4%	4.4%	17	53	1.6	25.1%	23.0%	2.1%	42.6%	1.3%	4.3%	0.9%	5.2%	97.4%	3,895,155	(104,845)	(52,599)	(52,246)	4,406,586	52,599	126,573	179,171
Used Vehicle - Indirect	18,500,000	1,637	684	n/a	0.6%	5.7%	5.7%	14	52	1.6	25.7%	22.5%	3.2%	42.2%	2.2%	5.1%	1.2%	6.3%	96.8%	17,900,864	(599,136)	(401,609)	(197,526)	20,934,228	401,609	768,125	1,169,734
Motorcycle	350,000	41	728	n/a	0.0%	4.7%	4.7%	16	46	1.4	27.3%	27.2%	0.1%	35.0%	0.0%	7.1%	1.1%	8.3%	95.4%	333,919	(16,081)	(91)	(15,989)	363,141	91	8,738	8,829
RV	850,000	92	750	n/a	0.0%	7.2%	7.2%	17	58	1.7	23.7%	23.6%	0.2%	61.1%	0.2%	6.4%	0.4%	6.8%	100.2%	851,792	1,792	(1,488)	3,281	1,006,370	1,488	48,898	50,387
Leases Receivable	60,000,000	1,825	768	n/a	0.0%	3.5%	3.5%	14	28	2.0	4.0%	4.0%	0.0%	0.0%	0.0%	3.3%	0.3%	3.6%	99.7%	59,805,143	(194,857)	-	(194,857)	67,710,246	-	3,908,343	3,908,343
MBL - Other Secured	60,000	2	n/a	n/a	0.0%	5.1%	5.1%	15	44	1.4	25.2%	25.2%	0.0%	65.0%	0.0%	6.4%	0.0%	6.4%	98.3%	58,990	(1,010)	(1)	(1,010)	67,064	1	1,612	1,612
MBL - Unsecured	55,000	3	n/a	n/a	0.0%	9.4%	9.4%	74	67	1.9	25.2%	25.2%	0.1%	100.0%	0.1%	10.0%	0.0%	10.0%	98.9%	54,422	(578)	(69)	(509)	70,768	69	5,935	6,005
Personal LOC	1,500,000	816	698	n/a	0.0%	11.3%	11.3%	234	44	1.5	25.5%	23.4%	2.1%	100.0%	3.2%	10.0%	1.5%	11.4%	97.0%	1,455,394	(44,606)	(48,128)	3,522	1,669,896	48,128	83,362	131,490
Signature	250,000	86	677	n/a	0.0%	9.9%	9.9%	14	30	1.1	26.2%	22.4%	3.8%	100.0%	5.2%	10.0%	1.7%	11.7%	93.6%	234,120	(15,880)	(13,117)	(2,763)	291,965	13,117	8,254	21,371
Share Secured	55,000	19	738	n/a	0.0%	3.6%	3.6%	19	30	1.0	25.2%	25.1%	0.1%	0.0%	0.0%	3.7%	0.0%	3.7%	99.9%	54,927	(73)	-	(73)	56,600	-	529	529
Other Secured	55,000	11	600	n/a	11.2%	2.7%	2.7%	69	49	1.5	27.1%	14.3%	12.8%	65.0%	10.6%	6.4%	3.9%	10.3%	80.7%	44,364	(10,636)	(5,818)	(4,818)	62,071	5,818	1,520	7,338
Credit Card	3,000,000	1,485	748	n/a	0.2%	8.3%	8.3%	n/a	59	1.7	25.8%	24.5%	1.2%	100.0%	1.9%	9.2%	0.5%	9.7%	96.4%	2,890,705	(109,295)	(55,907)	(53,388)	3,933,065	55,907	263,471	319,378
Student Loan	200,000	7	n/a	n/a	0.0%	5.1%	5.1%	10	230	5.2	13.4%	13.0%	0.4%	3.0%	0.1%	5.6%	0.0%	5.6%	97.8%	194,520	(5,480)	(137)	(5,344)	281,346	137	58,586	58,722
Total	181,075,000	8,651	741	38%	0.1%	4.3%	4.3%	26	82	2.5	14.7%	13.4%	1.2%	19.1%	0.7%	3.8%	0.5%	4.3%	99.4%	179,988,516	(1,086,484)	(1,188,864)	102,380	220,554,079	1,188,864	20,026,982	21,215,846

Loan Groupings used in Journal Entries

	Principal Balance	# of Loans	Fair Value %	Fair Value $	Difference	Credit Only Difference[1]	Discount Rate Difference[2]	Contractual Cash Flows	Non-Accretable Credit Losses	Non-Accretable Lost Interest	Total Non-Accretable Cash Flows
Fixed Rate Mortgage	36,000,000	326	101.6%	36,586,955	586,955	(135,755)	722,710	47,587,079	135,755	5,668,727	5,804,481
Home Equity	10,000,000	322	99.1%	9,912,094	(87,906)	(25,689)	(62,218)	11,929,719	25,689	1,188,641	1,214,330
HELOC	11,200,000	428	99.4%	11,133,192	(66,808)	(61,939)	(4,869)	13,451,758	61,939	812,414	874,353
Member Business Loans	21,115,000	132	99.0%	20,898,675	(216,325)	(254,799)	38,474	31,760,941	254,799	6,737,647	6,992,446
Auto Loans	36,500,000	3,061	97.5%	35,592,715	(907,285)	(585,997)	(321,288)	40,449,882	585,997	1,237,853	1,823,850
Other Consumer Loans	66,260,000	4,382	99.4%	65,864,885	(395,115)	(124,686)	(270,429)	75,374,701	124,686	4,381,700	4,506,386
Total	181,075,000	8,651	99.4%	179,988,516	(1,086,484)	(1,188,864)	102,380	220,554,079	1,188,864	20,026,982	21,215,846

[1] Credit Only Difference is referred to as the Credit Valuation Allowance

[2] Discount Rate Difference is referred to as the Discount Rate Valuation Allowance

For definitions of column headers, please see Appendix G

ABC Credit Union acquires
XYZ Credit Union
Journal Entries for ABC CU to adjust XYZ CU's Book Value (GAAP)

	Debit	Credit	Net Summary	5300 Reference	5300 Acct Code
Investments					
Available for Sale Securities	-	220,000			
Deposits in Commercial Banks, S&Ls, Savings Banks	6,000	-			
All Other Investments	104,000	-	(110,000)		
Loans					
Credit Adjustment					
Fixed Rate Mortgage	-	135,755			
Home Equity	-	25,689			
HELOC	-	61,939			
Member Business Loans	-	254,799			
Auto Loans	-	585,997			
Other Consumer Loans	-	124,686	(1,188,864)		
Discount Rate Adjustment					
Fixed Rate Mortgage	722,710	-			
Home Equity	-	62,218			
HELOC	277	5,146			
Member Business Loans	39,992	1,518			
Auto Loans	-	321,288			
Other Consumer Loans	6,803	277,232	102,380		
Total Loans and Leases - Loss Allowance	1,000,000	-	1,000,000		
Fixed Assets					
Land and Building	675,000	-	675,000		
Other Assets					
Core Deposit Intangible	2,500,000	-	2,500,000	Page 2, Line 31 a.	009D1
Shares/Deposits					
Share Certificates	-	125,000			
IRA/KEOGH Certificates	-	60,000	(185,000)		
Equity					
Equity (removal of existing equity accounts)	24,799,000				
Equity (record equity acquired in merger)		29,198,000		Page 4, Line 35	658A
			(4,399,000)		
Goodwill	1,605,484	-	1,605,484	Page 2, Line 31 b.	009D2
Bargain Purchase	-	-	-	Page 5, Line 17	431
	31,459,266	31,459,266	-		

GAAP

Acquirer's Equity before OCI Adjustment (Xyz CU Pre-Merger Equity)	60,000,000		
Plus: Acquirer's OCI Adjustment	(500,000)		
Total GAAP Equity	59,500,000		
Plus: Equity Acquired in Merger	29,198,000		
Plus: Bargain Purchase Gain	-		
Acquirer's Post-Merger GAAP Equity	88,698,000		

PCA Net Worth Merger Entries (Regulatory Only, Non-GAAP)

Acquirer's Regulatory Net Worth After Merger	88,698,000		
Less: OCI Adjustment	(500,000)		
Less: Equity Acquired in Merger	29,198,000	Page 4, Line 35	658A
Plus: Adjustments to Retained Earnings through Business Combinations	24,799,000	Page 11, Line 7 b.	1004B
Equity for PCA Net Worth Calculation	84,799,000		

WILARY WINN LLC

Interest Income Example - Used Vehicle - Direct

Nonaccretable Difference	Accretable Yield
442,016	759,881

Contractual Cashflows: Assuming no defaults, no prepays, etc. (Scheduled Balance through Scheduled P &I Payment)
SOP 03-3 Accounting (Beginning Carrying Amount through Ending Carrying Amount)
Wilary Winn Risk Management (Interest Expected to Be Collected through Total Interest Income)

Month	WAC	Remaining Balance	Principal Payment Expected to Be Collected	Voluntary Prepayment Expected to Be Collected	Interest Expected to Be Collected	Repo Principal Recoveries Expected to Be Collected	Total Cashflows Expected to Be Collected	Scheduled Balance	Scheduled Prin Payment	Scheduled Interest Payment	Scheduled P &I Payment	Cashflows Expected to Be Collected	Discounted Cashflows @ 3.8%	Discounted Cashflows @ 3.5%	Beginning Carrying Amount	Total Cashflows Expected to Be Collected	Interest Income	Reduction of Carrying Amount	Ending Carrying Amount	Interest Expected to Be Collected	Accretion (Amortization) of Discount Using SYD	Total Interest Income	Variance Between Methodologies
0		12,500,000						12,500,000															
1	3.5%	12,011,930	218,139	269,931	36,409	-	524,479	12,281,568	218,432	36,458	254,891	524,479	522,823	522,954	12,307,315	524,479	38,973	485,506	11,821,810	36,409	2,126	38,535	438
2	3.5%	11,539,325	213,673	258,933	34,939	-	507,545	12,062,498	219,070	35,821	254,891	507,545	504,345	504,597	11,821,810	507,545	37,436	470,109	11,351,701	34,939	2,086	37,024	411
3	3.5%	11,081,738	209,299	248,288	33,515	-	491,102	11,842,789	219,709	35,182	254,891	491,102	486,466	486,829	11,351,701	491,102	35,947	455,155	10,896,546	33,515	2,046	35,561	386
4	3.5%	10,638,740	205,014	237,985	32,137	-	475,136	11,622,440	220,349	34,541	254,891	475,136	469,165	469,633	10,896,546	475,136	34,506	440,631	10,455,916	32,137	2,005	34,143	363
5	3.5%	10,209,908	200,816	228,015	30,804	-	459,636	11,401,448	220,992	33,899	254,891	459,636	452,427	452,991	10,455,916	459,636	33,110	426,525	10,029,390	30,804	1,965	32,769	341
6	3.5%	9,794,834	196,705	218,369	29,514	-	444,587	11,179,812	221,637	33,254	254,891	444,587	436,233	436,886	10,029,390	444,587	31,760	412,827	9,616,563	29,514	1,925	31,439	321
7	3.5%	9,393,121	192,678	209,035	28,265	-	429,978	10,957,529	222,283	32,608	254,891	429,978	420,567	421,301	9,616,563	429,978	30,452	399,526	9,217,037	28,265	1,885	30,150	302
8	3.5%	9,004,381	188,733	200,007	27,057	-	415,797	10,734,597	222,931	31,959	254,891	415,797	405,412	406,221	9,217,037	415,797	29,187	386,609	8,830,428	27,057	1,845	28,902	285
9	3.5%	8,628,238	184,869	191,274	25,888	-	402,031	10,511,016	223,582	31,309	254,891	402,031	390,752	391,630	8,830,428	402,031	27,963	374,068	8,456,360	25,888	1,805	27,693	270
10	3.5%	8,264,326	181,084	182,827	24,758	-	388,670	10,286,782	224,234	30,657	254,891	388,670	376,573	377,513	8,456,360	388,670	26,778	361,891	8,094,469	24,758	1,765	26,523	256
11	3.5%	7,912,290	177,377	174,660	23,665	-	375,701	10,061,894	224,888	30,003	254,891	375,701	362,860	363,856	8,094,469	375,701	25,632	350,069	7,744,400	23,665	1,725	25,389	243
12	3.5%	7,571,781	173,746	166,763	22,607	-	363,116	9,836,351	225,544	29,347	254,891	363,116	349,597	350,644	7,744,400	363,116	24,524	338,592	7,405,808	22,607	1,685	24,292	232
13	3.5%	7,242,465	170,188	159,128	21,585	-	350,902	9,610,149	226,201	28,689	254,891	350,902	336,771	337,864	7,405,808	350,902	23,452	327,450	7,078,358	21,585	1,644	23,230	222
14	3.5%	6,924,013	166,704	151,748	20,597	-	339,049	9,383,288	226,861	28,030	254,891	339,049	324,369	325,503	7,078,358	339,049	22,415	316,634	6,761,724	20,597	1,604	22,201	213
15	3.5%	6,616,106	163,291	144,615	19,642	-	327,548	9,155,765	227,523	27,368	254,891	327,548	312,377	313,547	6,761,724	327,548	21,412	306,136	6,455,588	19,642	1,564	21,206	206
16	3.5%	6,318,436	159,948	137,722	18,718	-	316,389	8,927,579	228,186	26,704	254,891	316,389	300,782	301,984	6,455,588	316,389	20,443	295,946	6,159,642	18,718	1,524	20,243	200
17	3.5%	6,030,700	156,673	131,062	17,826	-	305,562	8,698,727	228,852	26,039	254,891	305,562	289,572	290,802	6,159,642	305,562	19,506	286,057	5,873,585	17,826	1,484	19,310	195
18	3.5%	5,752,605	153,466	124,628	16,964	-	295,059	8,469,207	229,520	25,371	254,891	295,059	278,736	279,989	5,873,585	295,059	18,600	276,459	5,597,126	16,964	1,444	18,408	192
19	3.5%	5,483,868	150,324	118,413	16,131	-	284,869	8,239,018	230,189	24,702	254,891	284,869	268,260	269,534	5,597,126	284,869	17,724	267,145	5,329,981	16,131	1,404	17,535	189
20	3.5%	5,224,210	147,246	112,411	15,327	-	274,985	8,008,158	230,860	24,030	254,891	274,985	258,135	259,425	5,329,981	274,985	16,878	258,106	5,071,875	15,327	1,364	16,691	188
21	3.5%	4,973,363	144,232	106,615	14,550	-	265,397	7,776,624	231,534	23,357	254,891	265,397	248,348	249,652	5,071,875	265,397	16,061	249,336	4,822,539	14,550	1,324	15,874	187
22	3.5%	4,731,064	141,279	101,020	13,800	-	256,098	7,544,415	232,209	22,682	254,891	256,098	238,891	240,204	4,822,539	256,098	15,271	240,827	4,581,711	13,800	1,283	15,083	188
23	3.5%	4,497,060	138,387	95,618	13,076	-	247,080	7,311,529	232,886	22,005	254,891	247,080	229,751	231,072	4,581,711	247,080	14,509	232,571	4,349,140	13,076	1,243	14,319	190
24	3.5%	4,271,102	135,553	90,405	12,376	-	238,335	7,077,964	233,565	21,325	254,891	238,335	220,919	222,244	4,349,140	238,335	13,772	224,562	4,124,578	12,376	1,203	13,580	193
25	3.5%	4,036,159	132,778	85,374	11,702	10,115	239,969	6,843,717	234,247	20,644	254,891	239,969	221,732	223,118	4,124,578	239,969	13,061	226,908	3,897,670	11,702	1,163	12,865	196
26	3.5%	3,809,467	130,060	80,521	11,051	9,706	231,337	6,608,787	234,930	19,961	254,891	231,337	213,081	214,467	3,897,670	231,337	12,343	218,995	3,678,675	11,051	1,123	12,174	169
27	3.5%	3,590,775	127,397	75,839	10,422	9,311	222,969	6,373,172	235,615	19,276	254,891	222,969	204,725	206,108	3,678,675	222,969	11,649	211,320	3,467,355	10,422	1,083	11,505	144
28	3.5%	3,379,842	124,789	71,324	9,816	8,928	214,857	6,136,870	236,302	18,588	254,891	214,857	196,654	198,032	3,467,355	214,857	10,980	203,877	3,263,478	9,816	1,043	10,859	121
29	3.5%	3,176,432	122,234	66,971	9,232	8,558	206,994	5,899,878	236,992	17,899	254,891	206,994	188,859	190,229	3,263,478	206,994	10,334	196,660	3,066,818	9,232	1,003	10,235	100
30	3.5%	2,980,317	119,731	62,774	8,668	8,199	199,373	5,662,195	237,683	17,208	254,891	199,373	181,331	182,692	3,066,818	199,373	9,712	189,661	2,877,157	8,668	963	9,631	81
31	3.5%	2,791,274	117,280	58,729	8,125	7,852	191,986	5,423,819	238,376	16,515	254,891	191,986	174,062	175,412	2,877,157	191,986	9,111	182,875	2,694,282	8,125	923	9,048	63
32	3.5%	2,609,087	114,879	54,831	7,602	7,517	184,828	5,184,748	239,071	15,819	254,891	184,828	167,043	168,381	2,694,282	184,828	8,532	176,296	2,517,986	7,602	882	8,484	48
33	3.5%	2,433,546	112,527	51,075	7,097	7,192	177,892	4,944,979	239,769	15,122	254,891	177,892	160,267	161,590	2,517,986	177,892	7,974	169,918	2,348,068	7,097	842	7,939	34
34	3.5%	2,264,447	110,223	47,458	6,611	6,878	171,171	4,704,511	240,468	14,423	254,891	171,171	153,725	155,033	2,348,068	171,171	7,436	163,735	2,184,333	6,611	802	7,413	22
35	3.5%	2,101,592	107,967	43,975	6,143	6,574	164,659	4,463,342	241,169	13,721	254,891	164,659	147,410	148,702	2,184,333	164,659	6,917	157,742	2,026,590	6,143	762	6,905	12
36	3.5%	1,944,788	105,756	40,622	5,692	6,280	158,351	4,221,469	241,873	13,018	254,891	158,351	141,316	142,589	2,026,590	158,351	6,418	151,934	1,874,656	5,692	722	6,414	4
37	3.5%	1,793,847	103,591	37,395	5,258	5,997	152,241	3,978,891	242,578	12,313	254,891	152,241	135,434	136,689	1,874,656	152,241	5,936	146,305	1,728,352	5,258	682	5,940	(3)
38	3.5%	1,648,589	101,470	34,290	4,840	5,722	146,323	3,735,605	243,286	11,605	254,891	146,323	129,758	130,993	1,728,352	146,323	5,473	140,849	1,587,503	4,840	642	5,482	(9)
39	3.5%	1,508,835	99,393	31,303	4,438	5,457	140,591	3,491,610	243,995	10,896	254,891	140,591	124,281	125,495	1,587,503	140,591	5,027	135,564	1,451,939	4,438	602	5,040	(13)
40	3.5%	1,374,415	97,358	28,430	4,052	5,200	135,040	3,246,903	244,707	10,184	254,891	135,040	118,998	120,190	1,451,939	135,040	4,598	130,442	1,321,497	4,052	562	4,613	(15)
41	3.5%	1,245,161	95,365	25,668	3,680	4,952	129,665	3,001,483	245,421	9,470	254,891	129,665	113,901	115,071	1,321,497	129,665	4,185	125,481	1,196,016	3,680	521	4,201	(17)
42	3.5%	1,120,912	93,412	23,014	3,322	4,713	124,461	2,755,346	246,136	8,754	254,891	124,461	108,985	110,131	1,196,016	124,461	3,787	120,674	1,075,342	3,322	481	3,804	(16)
43	3.5%	1,001,510	91,500	20,463	2,979	4,481	119,424	2,508,492	246,854	8,036	254,891	119,424	104,243	105,366	1,075,342	119,424	3,405	116,018	959,324	2,979	441	3,420	(15)
44	3.5%	886,801	89,627	18,014	2,649	4,258	114,547	2,260,917	247,574	7,316	254,891	114,547	99,671	100,770	959,324	114,547	3,038	111,509	847,815	2,649	401	3,050	(12)
45	3.5%	776,638	87,792	15,661	2,332	4,042	109,827	2,012,621	248,296	6,594	254,891	109,827	95,262	96,336	847,815	109,827	2,685	107,142	740,673	2,332	361	2,693	(8)
46	3.5%	670,877	85,994	13,403	2,027	3,834	105,259	1,763,600	249,021	5,870	254,891	105,259	91,011	92,061	740,673	105,259	2,345	102,913	637,759	2,027	321	2,348	(3)
47	3.5%	569,376	84,234	11,237	1,735	3,633	100,838	1,513,853	249,747	5,144	254,891	100,838	86,914	87,938	637,759	100,838	2,020	98,819	538,941	1,735	281	2,016	4
48	3.5%	472,000	82,509	9,159	1,454	3,438	96,561	1,263,378	250,475	4,415	254,891	96,561	82,965	83,963	538,941	96,561	1,707	94,855	444,086	1,454	241	1,695	12
49	3.5%	378,617	80,820	7,167	1,186	3,251	92,423	1,012,172	251,206	3,685	254,891	92,423	79,159	80,132	444,086	92,423	1,406	91,017	353,069	1,186	201	1,386	20
50	3.5%	289,098	79,166	5,257	928	3,070	88,420	760,233	251,939	2,952	254,891	88,420	75,492	76,438	353,069	88,420	1,118	87,302	265,767	928	160	1,088	30
51	3.5%	203,319	77,545	3,428	680	2,895	84,549	507,560	252,673	2,217	254,891	84,549	71,958	72,879	265,767	84,549	842	83,707	182,059	680	120	801	41
52	3.5%	121,158	75,957	1,677	444	2,727	80,804	254,150	253,410	1,480	254,891	80,804	68,554	69,449	182,059	80,804	577	80,228	101,831	444	80	524	53
53	3.5%	42,499	74,402	0	217	2,565	77,184	-	254,150	741	254,891	77,184	65,276	66,144	101,831	77,184	322	76,861	24,970	217	40	257	65
54	3.5%	-	-	0	0	2,408	2,408	-	-	-	-	2,408	2,030	2,058	24,970	2,408	79	2,329	22,641	0	-	0	79
55	3.5%	-	-	-	-	2,257	2,257	-	-	-	-	2,257	1,897	1,923	22,641	2,257	72	2,186	20,455	-	-	-	72
56	3.5%	-	-	-	-	2,112	2,112	-	-	-	-	2,112	1,769	1,794	20,455	2,112	65	2,047	18,408	-	-	-	65
57	3.5%	-	-	-	-	1,972	1,972	-	-	-	-	1,972	1,646	1,670	18,408	1,972	58	1,913	16,495	-	-	-	58
58	3.5%	-	-	-	-	1,837	1,837	-	-	-	-	1,837	1,529	1,551	16,495	1,837	52	1,784	14,711	-	-	-	52
59	3.5%	-	-	-	-	1,707	1,707	-	-	-	-	1,707	1,416	1,437	14,711	1,707	47	1,660	13,051	-	-	-	47
60	3.5%	-	-	-	-	1,581	1,581	-	-	-	-	1,581	1,308	1,328	13,051	1,581	41	1,540	11,511	-	-	-	41
61	3.5%	-	-	-	-	1,461	1,461	-	-	-	-	1,461	1,205	1,223	11,511	1,461	36	1,424	10,087	-	-	-	36
62	3.5%	-	-	-	-	1,345	1,345	-	-	-	-	1,345	1,105	1,123	10,087	1,345	32	1,313	8,774	-	-	-	32
63	3.5%	-	-	-	-	1,233	1,233	-	-	-	-	1,233	1,010	1,026	8,774	1,233	28	1,205	7,569	-	-	-	28
64	3.5%	-	-	-	-	1,126	1,126	-	-	-	-	1,126	919	934	7,569	1,126	24	1,102	6,467	-	-	-	24
65	3.5%	-	-	-	-	1,022	1,022	-	-	-	-	1,022	832	846	6,467	1,022	20	1,002	5,465	-	-	-	20
66	3.5%	-	-	-	-	923	923	-	-	-	-	923	749	762	5,465	923	17	906	4,560	-	-	-	17
67	3.5%	-	-	-	-	828	828	-	-	-	-	828	670	681	4,560	828	14	813	3,746	-	-	-	14
68	3.5%	-	-	-	-	736	736	-	-	-	-	736	593	604	3,746	736	12	724	3,022	-	-	-	12
69	3.5%	-	-	-	-	648	648	-	-	-	-	648	521	530	3,022	648	10	638	2,384	-	-	-	10
70	3.5%	-	-	-	-	563	563	-	-	-	-	563	451	459	2,384	563	8	556	1,829	-	-	-	8
71	3.5%	-	-	-	-	482	482	-	-	-	-	482	385	392	1,829	482	6	476	1,352	-	-	-	6
72	3.5%	-	-	-	-	404	404	-	-	-	-	404	322	328	1,352	404	4	400	953	-	-	-	4
73	3.5%	-	-	-	-	329	329	-	-	-	-	329	261	266	953	329	3	326	626	-	-	-	3
74	3.5%	-	-	-	-	258	258	-	-	-	-	258	204	208	626	258	2	256	371	-	-	-	2
75	3.5%	-	-	-	-	189	189	-	-	-	-	189	149	152	371	189	1	188	183	-	-	-	1
76	3.5%	-	-	-	-	123	123	-	-	-	-	123	97	99	183	123	1	123	60	-	-	-	1
77	3.5%	-	-	-	-	60	60	-	-	-	-	60	47	48	60	60	0	60	(0)	-	-	-	0
78	3.5%	-	-	-	-	0	0	-	-	-	-	0	0	0	(0)	0	(0)	0	(0)	-	-	-	(0)
Total			**7,095,183**	**5,084,534**	**694,533**	**192,946**	**13,067,196**		**12,500,000**	**1,009,212**	**13,509,212**		**12,307,315**	**12,364,711**		**13,067,196**	**759,881**	**12,307,315**		**694,533**	**57,396**	**751,929**	**7,952**
													WW RM Fair Value										
													98.5%	98.9%									

WILARY WINN LLC

ABC Credit Union
Fair Value Amortization Schedule

	Fixed Rate Mortgage	Home Equity	HELOC	Member Business Loans	Auto Loans	Other Consumer Loans	Total Loans	Deposits in Commercial Banks, S&Ls, Savings Banks	Income	Core Deposit Intangible	Share Certificates	IRA/KEOGH Certificates	Expense	Net
Credit Adjustment	135,755	25,689	61,939	254,799	585,997	124,686	1,188,864							
Interest Rate Adjustment	(722,710)	62,218	4,869	(38,474)	321,288	270,429	(102,380)	(6,000)	**(108,380)**	2,500,000	(125,000)	(60,000)	**2,315,000**	**(2,423,380)**
Fair Value Adjustment	(586,955)	87,906	66,808	216,325	907,285	395,115	1,086,484							
SYD Amortization (mos)	98	43	31	77	43	24		13		60	13	17		

Month	Fixed Rate Mortgage	Home Equity	HELOC	Member Business Loans	Auto Loans	Other Consumer Loans	Total Loans	Deposits in Commercial Banks, S&Ls, Savings Banks	**Income**	Core Deposit Intangible	Share Certificates	IRA/KEOGH Certificates	**Expense**	**Net**
0														
1	(14,600)	2,828	304	(987)	14,604	21,634	23,784	(857)	**22,927**	81,967	(17,857)	(6,667)	**57,443**	**(34,517)**
2	(14,451)	2,762	294	(974)	14,264	20,733	22,629	(791)	**21,838**	80,601	(16,484)	(6,275)	**57,843**	**(36,005)**
3	(14,302)	2,697	285	(961)	13,925	19,831	21,474	(725)	**20,749**	79,235	(15,110)	(5,882)	**58,243**	**(37,494)**
4	(14,153)	2,631	275	(948)	13,585	18,930	20,319	(659)	**19,660**	77,869	(13,736)	(5,490)	**58,642**	**(38,982)**
5	(14,004)	2,565	265	(935)	13,245	18,029	19,165	(593)	**18,571**	76,503	(12,363)	(5,098)	**59,042**	**(40,471)**
6	(13,855)	2,499	255	(922)	12,906	17,127	18,010	(527)	**17,482**	75,137	(10,989)	(4,706)	**59,442**	**(41,959)**
7	(13,706)	2,433	245	(910)	12,566	16,226	16,855	(462)	**16,393**	73,770	(9,615)	(4,314)	**59,841**	**(43,448)**
8	(13,557)	2,368	236	(897)	12,227	15,324	15,700	(396)	**15,304**	72,404	(8,242)	(3,922)	**60,241**	**(44,937)**
9	(13,408)	2,302	226	(884)	11,887	14,423	14,545	(330)	**14,216**	71,038	(6,868)	(3,529)	**60,641**	**(46,425)**
10	(13,259)	2,236	216	(871)	11,547	13,521	13,390	(264)	**13,127**	69,672	(5,495)	(3,137)	**61,040**	**(47,914)**
11	(13,110)	2,170	206	(858)	11,208	12,620	12,235	(198)	**12,038**	68,306	(4,121)	(2,745)	**61,440**	**(49,402)**
12	(12,961)	2,105	196	(846)	10,868	11,719	11,081	(132)	**10,949**	66,940	(2,747)	(2,353)	**61,840**	**(50,891)**
13	(12,812)	2,039	187	(833)	10,528	10,817	9,926	(66)	**9,860**	65,574	(1,374)	(1,961)	**62,239**	**(52,379)**
14	(12,663)	1,973	177	(820)	10,189	9,916	8,771	-	**8,771**	64,208	-	(1,569)	**62,639**	**(53,868)**
15	(12,514)	1,907	167	(807)	9,849	9,014	7,616	-	**7,616**	62,842	-	(1,176)	**61,665**	**(54,049)**
16	(12,365)	1,842	157	(794)	9,510	8,113	6,461	-	**6,461**	61,475	-	(784)	**60,691**	**(54,230)**
17	(12,216)	1,776	147	(782)	9,170	7,211	5,306	-	**5,306**	60,109	-	(392)	**59,717**	**(54,411)**
18	(12,068)	1,710	137	(769)	8,830	6,310	4,152	-	**4,152**	58,743	-	-	**58,743**	**(54,592)**
19	(11,919)	1,644	128	(756)	8,491	5,409	2,997	-	**2,997**	57,377	-	-	**57,377**	**(54,380)**
20	(11,770)	1,578	118	(743)	8,151	4,507	1,842	-	**1,842**	56,011	-	-	**56,011**	**(54,169)**
21	(11,621)	1,513	108	(730)	7,811	3,606	687	-	**687**	54,645	-	-	**54,645**	**(53,958)**
22	(11,472)	1,447	98	(717)	7,472	2,704	(468)	-	**(468)**	53,279	-	-	**53,279**	**(53,747)**
23	(11,323)	1,381	88	(705)	7,132	1,803	(1,623)	-	**(1,623)**	51,913	-	-	**51,913**	**(53,535)**
24	(11,174)	1,315	79	(692)	6,793	901	(2,778)	-	**(2,778)**	50,546	-	-	**50,546**	**(53,324)**
25	(11,025)	1,250	69	(679)	6,453	-	(3,932)	-	**(3,932)**	49,180	-	-	**49,180**	**(53,113)**
26	(10,876)	1,184	59	(666)	6,113	-	(4,186)	-	**(4,186)**	47,814	-	-	**47,814**	**(52,000)**
27	(10,727)	1,118	49	(653)	5,774	-	(4,439)	-	**(4,439)**	46,448	-	-	**46,448**	**(50,887)**
28	(10,578)	1,052	39	(641)	5,434	-	(4,693)	-	**(4,693)**	45,082	-	-	**45,082**	**(49,775)**
29	(10,429)	987	29	(628)	5,094	-	(4,946)	-	**(4,946)**	43,716	-	-	**43,716**	**(48,662)**
30	(10,280)	921	20	(615)	4,755	-	(5,200)	-	**(5,200)**	42,350	-	-	**42,350**	**(47,549)**
31	(10,131)	855	10	(602)	4,415	-	(5,453)	-	**(5,453)**	40,984	-	-	**40,984**	**(46,437)**
32	(9,982)	789	-	(589)	4,076	-	(5,706)	-	**(5,706)**	39,617	-	-	**39,617**	**(45,324)**
33	(9,833)	723	-	(577)	3,736	-	(5,950)	-	**(5,950)**	38,251	-	-	**38,251**	**(44,201)**
34	(9,684)	658	-	(564)	3,396	-	(6,194)	-	**(6,194)**	36,885	-	-	**36,885**	**(43,079)**
35	(9,535)	592	-	(551)	3,057	-	(6,437)	-	**(6,437)**	35,519	-	-	**35,519**	**(41,956)**
36	(9,386)	526	-	(538)	2,717	-	(6,681)	-	**(6,681)**	34,153	-	-	**34,153**	**(40,834)**
37	(9,237)	460	-	(525)	2,377	-	(6,924)	-	**(6,924)**	32,787	-	-	**32,787**	**(39,711)**
38	(9,088)	395	-	(512)	2,038	-	(7,168)	-	**(7,168)**	31,421	-	-	**31,421**	**(38,589)**
39	(8,939)	329	-	(500)	1,698	-	(7,412)	-	**(7,412)**	30,055	-	-	**30,055**	**(37,466)**
40	(8,790)	263	-	(487)	1,359	-	(7,655)	-	**(7,655)**	28,689	-	-	**28,689**	**(36,344)**
41	(8,641)	197	-	(474)	1,019	-	(7,899)	-	**(7,899)**	27,322	-	-	**27,322**	**(35,221)**
42	(8,492)	132	-	(461)	679	-	(8,142)	-	**(8,142)**	25,956	-	-	**25,956**	**(34,099)**
43	(8,343)	66	-	(448)	340	-	(8,386)	-	**(8,386)**	24,590	-	-	**24,590**	**(32,976)**
44	(8,194)	-	-	(436)	-	-	(8,630)	-	**(8,630)**	23,224	-	-	**23,224**	**(31,854)**
45	(8,045)	-	-	(423)	-	-	(8,468)	-	**(8,468)**	21,858	-	-	**21,858**	**(30,326)**
46	(7,896)	-	-	(410)	-	-	(8,306)	-	**(8,306)**	20,492	-	-	**20,492**	**(28,798)**
47	(7,747)	-	-	(397)	-	-	(8,144)	-	**(8,144)**	19,126	-	-	**19,126**	**(27,270)**
48	(7,598)	-	-	(384)	-	-	(7,982)	-	**(7,982)**	17,760	-	-	**17,760**	**(25,742)**
49	(7,449)	-	-	(372)	-	-	(7,821)	-	**(7,821)**	16,393	-	-	**16,393**	**(24,214)**
50	(7,300)	-	-	(359)	-	-	(7,659)	-	**(7,659)**	15,027	-	-	**15,027**	**(22,686)**
51	(7,151)	-	-	(346)	-	-	(7,497)	-	**(7,497)**	13,661	-	-	**13,661**	**(21,158)**
52	(7,002)	-	-	(333)	-	-	(7,335)	-	**(7,335)**	12,295	-	-	**12,295**	**(19,630)**
53	(6,853)	-	-	(320)	-	-	(7,173)	-	**(7,173)**	10,929	-	-	**10,929**	**(18,102)**
54	(6,704)	-	-	(307)	-	-	(7,012)	-	**(7,012)**	9,563	-	-	**9,563**	**(16,575)**
55	(6,555)	-	-	(295)	-	-	(6,850)	-	**(6,850)**	8,197	-	-	**8,197**	**(15,047)**
56	(6,406)	-	-	(282)	-	-	(6,688)	-	**(6,688)**	6,831	-	-	**6,831**	**(13,519)**
57	(6,257)	-	-	(269)	-	-	(6,526)	-	**(6,526)**	5,464	-	-	**5,464**	**(11,991)**
58	(6,108)	-	-	(256)	-	-	(6,364)	-	**(6,364)**	4,098	-	-	**4,098**	**(10,463)**
59	(5,959)	-	-	(243)	-	-	(6,203)	-	**(6,203)**	2,732	-	-	**2,732**	**(8,935)**
60	(5,810)	-	-	(231)	-	-	(6,041)	-	**(6,041)**	1,366	-	-	**1,366**	**(7,407)**
61	(5,661)	-	-	(218)	-	-	(5,879)	-	**(5,879)**	-	-	-	**-**	**(5,879)**
62	(5,512)	-	-	(205)	-	-	(5,717)	-	**(5,717)**	-	-	-	**-**	**(5,717)**
63	(5,363)	-	-	(192)	-	-	(5,556)	-	**(5,556)**	-	-	-	**-**	**(5,556)**
64	(5,214)	-	-	(179)	-	-	(5,394)	-	**(5,394)**	-	-	-	**-**	**(5,394)**
65	(5,065)	-	-	(167)	-	-	(5,232)	-	**(5,232)**	-	-	-	**-**	**(5,232)**
66	(4,916)	-	-	(154)	-	-	(5,070)	-	**(5,070)**	-	-	-	**-**	**(5,070)**
67	(4,767)	-	-	(141)	-	-	(4,908)	-	**(4,908)**	-	-	-	**-**	**(4,908)**
68	(4,618)	-	-	(128)	-	-	(4,747)	-	**(4,747)**	-	-	-	**-**	**(4,747)**
69	(4,469)	-	-	(115)	-	-	(4,585)	-	**(4,585)**	-	-	-	**-**	**(4,585)**
70	(4,320)	-	-	(102)	-	-	(4,423)	-	**(4,423)**	-	-	-	**-**	**(4,423)**
71	(4,171)	-	-	(90)	-	-	(4,261)	-	**(4,261)**	-	-	-	**-**	**(4,261)**
72	(4,023)	-	-	(77)	-	-	(4,099)	-	**(4,099)**	-	-	-	**-**	**(4,099)**
73	(3,874)	-	-	(64)	-	-	(3,938)	-	**(3,938)**	-	-	-	**-**	**(3,938)**
74	(3,725)	-	-	(51)	-	-	(3,776)	-	**(3,776)**	-	-	-	**-**	**(3,776)**
75	(3,576)	-	-	(38)	-	-	(3,614)	-	**(3,614)**	-	-	-	**-**	**(3,614)**
76	(3,427)	-	-	(26)	-	-	(3,452)	-	**(3,452)**	-	-	-	**-**	**(3,452)**
77	(3,278)	-	-	(13)	-	-	(3,290)	-	**(3,290)**	-	-	-	**-**	**(3,290)**
78	(3,129)	-	-	-	-	-	(3,129)	-	**(3,129)**	-	-	-	**-**	**(3,129)**
79	(2,980)	-	-	-	-	-	(2,980)	-	**(2,980)**	-	-	-	**-**	**(2,980)**
80	(2,831)	-	-	-	-	-	(2,831)	-	**(2,831)**	-	-	-	**-**	**(2,831)**
81	(2,682)	-	-	-	-	-	(2,682)	-	**(2,682)**	-	-	-	**-**	**(2,682)**
82	(2,533)	-	-	-	-	-	(2,533)	-	**(2,533)**	-	-	-	**-**	**(2,533)**
83	(2,384)	-	-	-	-	-	(2,384)	-	**(2,384)**	-	-	-	**-**	**(2,384)**
84	(2,235)	-	-	-	-	-	(2,235)	-	**(2,235)**	-	-	-	**-**	**(2,235)**
85	(2,086)	-	-	-	-	-	(2,086)	-	**(2,086)**	-	-	-	**-**	**(2,086)**
86	(1,937)	-	-	-	-	-	(1,937)	-	**(1,937)**	-	-	-	**-**	**(1,937)**
87	(1,788)	-	-	-	-	-	(1,788)	-	**(1,788)**	-	-	-	**-**	**(1,788)**
88	(1,639)	-	-	-	-	-	(1,639)	-	**(1,639)**	-	-	-	**-**	**(1,639)**
89	(1,490)	-	-	-	-	-	(1,490)	-	**(1,490)**	-	-	-	**-**	**(1,490)**
90	(1,341)	-	-	-	-	-	(1,341)	-	**(1,341)**	-	-	-	**-**	**(1,341)**
91	(1,192)	-	-	-	-	-	(1,192)	-	**(1,192)**	-	-	-	**-**	**(1,192)**
92	(1,043)	-	-	-	-	-	(1,043)	-	**(1,043)**	-	-	-	**-**	**(1,043)**
93	(894)	-	-	-	-	-	(894)	-	**(894)**	-	-	-	**-**	**(894)**
94	(745)	-	-	-	-	-	(745)	-	**(745)**	-	-	-	**-**	**(745)**
95	(596)	-	-	-	-	-	(596)	-	**(596)**	-	-	-	**-**	**(596)**
96	(447)	-	-	-	-	-	(447)	-	**(447)**	-	-	-	**-**	**(447)**
97	(298)	-	-	-	-	-	(298)	-	**(298)**	-	-	-	**-**	**(298)**
98	(149)	-	-	-	-	-	(149)	-	**(149)**	-	-	-	**-**	**(149)**
Total	**(722,710)**	**62,218**	**4,869**	**(38,474)**	**321,288**	**270,429**	**(102,380)**	**(6,000)**	**(108,380)**	**2,500,000**	**(125,000)**	**(60,000)**	**2,315,000**	**(2,423,380)**

Fair Value Loan Valuation Definitions

Principal Balance:	Outstanding principal balance on the loan as of the valuation date.
# of Loans:	Count of loans
Avg FICO:	Weighted Average current FICO credit score. Weighted by balance and only loans with a valid credit score are included in the weighting.
Avg LTV*:	Weighted Average Loan to Value (LTV). Outstanding loan balance divided by the current appraised home value. Average is weighted by balance and only loans with a valid LTV are included in the weighting. The LTV shown here on the loans in second position is a Combined LTV which is the sum of the 1st mortgage plus the 2nd mortgage balance divided by the current appraised value.
WAC:	Weighted Average Coupon. This is the contractual rate of interest on the loan.
Age:	Number of months elapsed since the loan was originated.
WAM:	Weighted Average Maturity. Number of months remaining until the loan is due on the contractual loan payment schedule.
Avg Life:	The average number of years that the Principal Balance will remain outstanding. This calculated amount indicates how many years it will take to repay half of the outstanding Principal Balance. This calculation is dependent on the loan's scheduled amortization and our CPR% assumption.
CPR %:	Conditional Prepayment Rate. Annual % of expected voluntary and involuntary payoffs (defaults). CRR% plus CDR% = CPR%. CPR% compares to the PSA (Public Securities Association) standard prepayment speed and PSA of 100% equates to a 6% CPR% in month 30 and beyond. CPR% is also similar to an annualized SMM (Single Monthly Mortality) rate. A CPR% of 10% roughly indicates that 10% of the starting Principal Balance will be paid off by the end of a one year time period.
CRR %:	Conditional Repayment Rate. Annual amount of expected voluntary payoffs as a percentage of the principal amount outstanding at the beginning of the year.

Appendix G

CDR %:	Conditional Default Rate. Annual amount of expected defaults as a percentage of the principal amount outstanding at the beginning of the year.
Severity %:	Loss Severity expected on a loan that does go into default. This is equal to the liquidated Principal Balance minus any recovered amount divided by the Principal Balance. Severity % is the inverse of a recovery rate.
Future Loss %:	Future expected net cumulative losses expressed as a % of current Principal Balance.
Discount Rate:	Rate used to present value the expected gross cashflows back to the valuation date. The rate on used on the top two FICO score buckets (>719) are the observable current market rates. For FICO scores that are below 720, we have used a build-up methodology. Please see the report for more details on this methodology.
Fair Value %:	Fair Value dollar amount expressed as a percent of the current Principal Balance.
Fair Value $:	Present value of the expected future cashflows. Expected future gross cashflows are dependent on the contractual terms of the loan (interest rate, term), our repayment assumptions (CRR %), our default assumption (CDR %), and our loss Severity % assumptions. For accounting purposes, the gross cash flows are considered to be a single best estimate assumption. The gross cashflows are discounted using the Discount Rate.
Difference:	Fair Value $ minus Principal Balance. This difference is broken out further into a Credit Only Difference and a Discount Rate Difference.
Credit Only Difference:	The Fair Value Difference that arises only from our credit assumptions (CDR % and Severity %). This number is the total expected lifetime net losses discounted by the WAC on the loans. To estimate an annualized loss amount, take this Credit Only Difference amount divided by the Avg Life.
Discount Rate Difference:	The Fair Value Difference that arises only from our Discount Rate assumption. A positive Discount Rate Difference means that the interest rate (WAC) on the loans is higher than the current market interest rate environment. If WAC and Discount Rate were exactly the same, the Discount Rate Difference would be zero.
Contractual Cashflows:	The scheduled cashflows expected if the loan did not prepay or default.
Non-Accretable Cashflows:	The variance between the Contractual Cashflows and the total cashflows expected to collected. Total cashflows expected to be collected do take into account prepay, default, and loss assumptions.